The New Wyoming Statutory Close Corporation Supplement; Should Your Corporation Elect Statutory Close Corporation Status

James Bell Gilpin

William K. Rounsborg

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THE NEW WYOMING
STATUTORY CLOSE CORPORATION SUPPLEMENT;
SHOULD YOUR CORPORATION ELECT
STATUTORY CLOSE CORPORATION STATUS?

Effective January 1, 1990, Wyoming joined a host of states which have enacted special legislation providing additional authorization or regulation for close corporations, sometimes referred to as "statutory close corporations." The Wyoming Statute, known as the Wyoming Statutory Close Corporation Supplement (Supplement) follows the format of the Model Close Corporation Supplement, and like other close corporation statutes recognizes the special needs of the close corporation.

The Supplement provides Wyoming attorneys with an alternative to the new "Wyoming Business Corporation Act" (Act), when incorporating family-owned or closely held businesses. While the Close Corporation Supplement is specifically designed for closely-held corporations, the attorney should compare its special provisions with the provisions of the Wyoming Business Corporation Act, in light of his client's needs, before deciding to incorporate under either the Supplement or the Act.

Prior to special close corporation legislation, when a lawyer incorporated such a business he did so under the general corporation law of the state, turning out a small replica of a public issue corporation. If the lawyer failed to recognize the special needs of the close corporation, he expended little effort to eliminate any of the traditional corporate attributes which were unattractive or undesirable to a small closely-held business. Even if the lawyer recognized the special needs of such an enterprise, he had to individually tailor the corporate form to the needs of the particular enterprise, making incorporation less cost effective for a small business.

Initially, it is important to recognize the distinctions between closely-held and publicly-held corporations. Close corporations are often existing family-owned or closely held businesses which incorporate to enjoy the benefits of limited liability, or the special tax advantages provided to corporations. Closely-held corporations differ from publicly-held corporations in that: 1) they have a relatively small number of

2. Id. § 17-17-101.

Election of close corporation status is distinct from election of S Corporation status under the tax code. Election of close corporation status does not automatically give rise to S Corporation tax status. The drafters of the Wyoming Supplement, however, restricted the number of shareholders in a close corporation to thirty-five in part to
shareholders; 2) the shareholders are active in the management of corporate affairs; 3) there is no established market for the corporate shares; and 4) the corporation’s shares are not freely transferable. Close corporations are often run in an informal manner and the shareholders occupy overlapping roles serving as owners, directors and management. Commentators have long recognized these distinctions and have advocated enactment of special legislation to deal with the unique needs of close corporations.\textsuperscript{7}

To deal with the special needs of close corporations, various states enacted special provisions for close corporations.\textsuperscript{8} Neither the substance nor the form of these provisions is uniform.\textsuperscript{9} Some states have adopted provisions which are specifically applicable to close corporations and are gathered in a special supplement.\textsuperscript{10} Others have adopted provisions which are dispersed throughout the corporate code.\textsuperscript{11} The Wyoming Supplement adopts the prior format, providing provisions, contained in a separate supplement, which are specifically applicable to “statutory close corporations.”\textsuperscript{12}

Generally special close corporation provisions apply only to defined “statutory close corporations.”\textsuperscript{13} A variety of standards are employed to determine which corporations are subject to, or may elect, “statutory close corporation” status.\textsuperscript{14} These standards often include the number of shareholders, the presence of restrictions on the transfer of shares, and the absence of any public offering of securities or a listing on a


There are significant differences between the eligibility for close corporation status under the Wyoming Close Corporation Supplement and Subchapter S tax status under the Internal Revenue Code. For example, to be eligible for S Corporation tax status, the shareholders of the corporation must be individuals, not other corporations or partnerships. 26 U.S.C. § 1361 (b)(1)(B) (1982). Also, an S Corporation cannot have more than one class of stock. \textit{Id.} § 1361 (b)(1)(D). A lawyer should not rely on the Supplement independently if the corporation also seeks S Corporation tax status. For a complete discussion of the S Corporation election, see, e.g., L. Bravenec, \textit{Federal Taxation of S Corporations and Shareholders} (2d ed. 1988).

9. \textit{Id.} § 1.15.
10. \textit{Id.}
11. \textit{Id.}
12. WYO. STAT. § 17-17-103 (1989). A statutory close corporation is a corporation whose articles of incorporation contain a statement that the corporation is a statutory close corporation. \textit{Id.}
13. \textit{Id.}
14. O’Neal, \textit{supra} note 9, at § 1.15.
national securities exchange. The Wyoming Supplement limits "statutory close corporation" status to corporations which elect such status, and have thirty-five or fewer shareholders.

Once a corporation is subject to, or elects, close corporation status, it is entitled to take advantage of the special provisions which are tailored to meet its needs. These provisions allow increased flexibility in structuring the corporation; provide greater certainty that agreements structuring the corporate operation will be enforced; reduce the amount of drafting required to accomplish the desired management and control structure; and recognize the needs of minority shareholders to a greater extent.

Despite these special provisions, many corporations eligible for statutory close corporation status do not elect such status. One reason for this is the general flexibility and permissiveness now allowed by most general corporation statutes. Also, there may be more devel-

15. Id.
16. To elect "statutory close corporation" status, the corporation must amend its articles of incorporation to include a statement that the corporation is a statutory close corporation. Wyo. Stat. § 17-14-103(b). Both existing corporations, as well as corporations formed after the statutes effective date are eligible for close corporation status. Id. If the corporation was formed prior to January 1, 1990, then the amendment must be approved by all of the shareholders. Id. For corporations formed after January 1, 1990, the amendment must be approved by at least two-thirds (2/3) of the shareholders. Id. A dissenting shareholder is entitled to assert dissenters' rights under Wyo. Stat. §§ 17-16-1301 to 17-16-1331. Id.
17. If a corporation elects close corporation status it must make certain disclosures. The shareholders must receive notice that their shares are subject to transfer restrictions and that their rights and liabilities differ from those of other corporate shareholders. Id. § 17-17-110 (1989). The following statement must appear conspicuously on each share certificate issued by a statutory close corporation: "[t]he rights of shareholders in a statutory close corporation may differ materially from the rights of shareholders of other corporations." Copies of the articles of incorporation and bylaws, shareholders' agreements, and other documents, any of which may restrict or affect the voting rights, may be obtained by a shareholder on written request to the corporation. Id. at § 17-17-110(a).
18. Model Close Corporation Supplement § 10 Official Comment (1984). The Wyoming Supplement provides that: [a] person claiming an interest in shares of a statutory close corporation which has complied with the notice requirement. . . . is bound by the documents referred to in the notice. Id. § 17-17-110(d). "A person claiming an interest in shares of a . . . corporation which has not complied with the notice requirement . . . is bound by any documents of which he, or a person through whom he claims, has knowledge or notice. Id.
19. Wyo. Stat. § 17-17-103(b) (1989). This differs from the Model Statutory Close Corporation Supplement in which corporations which have fifty (50) or fewer shareholders are eligible for close corporation status. Model Close Corporation Supplement § 103.

O'Neal, supra note 9, at § 1.15.
oped caselaw under the general corporate statutes, providing greater certainty as to the court’s interpretation of the statute.

In light of the fact that Wyoming has enacted a new Business Corporation Act which follows the format of the Revised Model Business Corporation Act, allowing greater flexibility, it is important to compare the provisions of the Supplement to those provided by the Act. While the Supplement provisions are not designed to meet the needs of all business organizations, its provisions offer specific advantages to many closely held enterprises. This comment will set forth the Supplement provisions providing advantages to closely held corporations and compare them to the provisions under the Wyoming Business Corporation Act. This comparison reveals the advantages offered by the Supplement’s special provisions to closely held corporations electing close corporation status.

ELECTION OF CLOSE CORPORATION STATUS

Since “statutory close corporation” status is subject to election under the Wyoming Supplement, the choice to elect such status should not be made prior to comparing the advantages offered by the Supplement with those provided by the Wyoming Business Corporation Act.21 The Wyoming Supplement is specifically tailored to meet the needs of close corporations, and specifically permits some managerial structures not permitted by the Wyoming Business Corporation Act.22 The advantages of the Supplement can be grouped into three main categories: 1) provisions permitting flexibility in management; 2) limitations of the transfer of stock; and 3) remedies available to shareholders.

PROVISIONS PERMITTING FLEXIBILITY

Close corporations are often operated on an informal basis. The shareholders own the corporation and are also involved in its day to day operation. Often, these shareholders are not sophisticated businessmen accustomed to corporate boardrooms or formal meetings. Under these circumstances traditional corporate law strangles the management of a close corporation. To deal with this problem the Wyoming Supplement includes provisions which specifically permit flexibility in the management of a close corporation. These provisions explicitly

Shapiro, The Statutory Close Corporation: A Critique and a Corporate Planning Alternative, 36 Md. L. Rev. 289, 301 (1976). “[T]he general corporate law may actually aid the unsophisticated practitioner in assessing and implementing the range of planning options most suitable for achieving the client’s objective” by providing a broad checklist of permissible provisions for inclusion in the articles of incorporation. Id.


22. Wyo. Stat. § 17-17-120 (a) (1989). All the shareholders of a statutory close corporation may agree in writing to regulate the exercise of the corporate powers and the management of the business and affairs of the corporation or the relationship among the shareholders of the corporation. Id.
authorize shareholder agreements, and specifically allow the shareholders to eliminate the board of directors, corporate bylaws, and annual meetings. The provisions also shield the shareholders from personal liability if the corporation fails to follow corporate formalities.

A. Shareholder Agreements.

Proponents of close corporation statutes cite the statutes approval of shareholder agreements as the chief advantage to electing “statutory close corporation” status. Shareholder agreements are intended to play a role similar to that of a partnership agreement. Under traditional corporate law close corporations were required to operate within statutory norms. This prevented shareholders from infringing upon the directors’ authority to manage the corporation.

In small family owned or closely-held corporation such an arrangement is unrealistic. In these corporations, shareholder agreements are often necessary to protect the financial interests of close corporation shareholders. While the shareholders of a public issue corporation may readily sell his shares on the open market if the management fails to use, in his opinion, sound business judgment, a shareholder in a closely held corporation often has a large portion of his capital invested in the business and no ready market exists to sell his shares should he desire. Absent a shareholder agreement, specifically enforced by the courts, a minority shareholder may find himself without a modicum of control and at the mercy of an oppressive or ignorant majority.

23. Id. § 17-17-120.
24. Id. § 17-17-121.
25. Id. § 17-17-122.
26. Id. § 17-17-123.
27. Id. § 17-17-125.

Examples of provisions which may be included in an agreement are: (1) The management of the business and affairs of the corporation in whole or part may be by or under the direction of all the shareholders of the corporation or by or under the direction of one or more shareholders or third parties selected by the shareholders; (2) One or more shareholders may be given the power to dissolve the corporation at will or upon the occurrence of a specified event or contingency; (3) The manner of exercising or dividing voting power by the shareholders or directors may be established, and the use of director as well as shareholder proxies may be authorized; (4) The terms and conditions of employment of any officer or employee by the corporation may be established; (5) The identity of the directors and officers of the corporation may be established; (6) The payment of dividends or division of profits may be established; (7) Issues as to which the shareholders or directors are deadlocked may be made subject to arbitration, or arbitration may be required for any issue of disagreement between a shareholder in his capacity as a shareholder, director, officer, or employee and the corporation, or the other shareholders. MODEL CLOSE CORPORATION SUPPLEMENT § 20 Official Comment.

29. Hochstetler, supra note 5, at 904-05.
31. Hochstetler, supra note 5, at 853.
The Wyoming Supplement allows shareholders to regulate the business and affairs of the close corporation or control relations among shareholders by written agreement.\textsuperscript{32} The Supplement explicitly permits "statutory close corporation" shareholders to enter into agreements regulating the exercise of corporate powers, and the management of corporate business and affairs.\textsuperscript{33} Shareholders may agree to eliminate the board of directors,\textsuperscript{34} restrict the board's discretion and powers,\textsuperscript{35} treat the corporation as a partnership,\textsuperscript{36} or create a relationship which would otherwise be appropriate only among partners.\textsuperscript{37}

The only requirement for a valid shareholder agreement is that all of the shareholders must agree in writing.\textsuperscript{38} Unanimity is required due to the unusual nature of an agreement that so radically alters the normal corporate structure.\textsuperscript{39}

While the Wyoming Supplement explicitly authorizes shareholder agreements, the Wyoming Business Corporation Act does not. The validity of such agreements under the Act can be support by caselaw indicating a increased tolerance toward the agreements by the courts.\textsuperscript{40} Although, in the past, courts looked upon agreements which violated the statutory scheme with disfavor, they have since allowed greater flexibility and latitude in the scope of shareholder agreements.\textsuperscript{41} Shareholder agreements which technically violate the letter of general corporate acts have been upheld in light of certain circumstances, i.e., where no apparent public injury results, in the absence of a complaining minority interest, and where no apparent prejudice results to corporate creditors.\textsuperscript{42}

In addition to caselaw, the Act itself seems to support such agreements. Under the Act the board of directors has the power to direct or oversee the direction of the business and affairs of the corporation, subject to any limitation set forth in the articles of incorporation.\textsuperscript{43} This provision should authorize any variation of the statutory scheme as long as a statement to that effect appears in the articles of incorporation.\textsuperscript{44} The Act does not, however, specifically prescribe the limits or scope of such variations. Therefore, the interpretation and validity of such agreements is left to the courts discretion.

While both the Supplement and the Act appear to authorize shareholder agreements, the Supplement explicitly approves such agree-

\textsuperscript{32} \textit{Wy. Stat.} \textsection 17-17-120 (1989).
\textsuperscript{33} \textit{Id.} \textsection 17-17-120(a).
\textsuperscript{34} \textit{Id.} \textsection 17-17-120(b)(i).
\textsuperscript{35} \textit{Id.} \textsection 17-17-120(b)(ii).
\textsuperscript{36} \textit{Id.} \textsection 17-17-120(b)(iii).
\textsuperscript{37} \textit{Id.} \textsection 17-17-120(b)(iv).
\textsuperscript{38} \textit{Id.} \textsection 17-17-120(a).
\textsuperscript{39} \textit{Model Close Corporation Supplement} \textsection 20 Official Comment (1984).
\textsuperscript{40} \textit{See, e.g.}, Galler v. Galler, 203 N.E.2d 577 (Ill. 1964).
\textsuperscript{41} \textit{Id.}
\textsuperscript{42} \textit{Id.}
\textsuperscript{43} \textit{Wy. Stat.} \textsection 17-16-801(b) (1989) (emphasis added).
\textsuperscript{44} \textit{Id.}
ments. This authority provides the practitioner with greater certainty that drafted agreements will be construed as valid and enforceable by the courts. Therefore, if the attorney wishes to use shareholder agreements to alter the control, structure or management of a close corporation, the Supplement offers a clear advantage — explicit authorization.

B. Elimination of the Board of Directors.

Structuring the management and control of a closely held corporation is important to protect the shareholders’ financial interest. While a shareholder agreement provides one means, the Supplement allows other measures which are also valuable tools to manage and control the corporation. One such measure is to eliminate the board of directors or restrict the powers and discretion of the board.45

Generally the business and affairs of a corporation are managed under the direction of a board of directors.46 In the typical close corporation there is no division between ownership and management, characteristic of publicly held corporations.47 The shareholders are often the officers; and expect to manage the corporation through direct participation, rather than through a board of directors.48 Therefore, there is no need for a board of directors.49

The Supplement allows the shareholders of a “statutory close corporation” to eliminate or restrict the powers or discretion of the board of directors.50 If the shareholders desire to eliminate the board of directors, they must all enter a written agreement to that effect.51 In addition, the corporation’s articles of incorporation must be amended providing a statement to the effect that the corporation will operate without a board of directors.52

The Supplement provides that after the board of directors is eliminated, its responsibilities shift to the shareholders.53 Thereafter, all cor-

45. Id. § 17-17-120(b)(i)&(ii).
46. Id. § 17-16-801. The Act provides that “all corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors.” Id.
47. Hochstetler, supra note 5, at 853.
48. Id.
49. Winer, Proposing a New York Close Corporation Law, 28 CORNELL L. Q. 313, 316 (1943). A board [of directors in a close corporation] ... is generally but a superfluous complication. On the one hand, five stockholders may well manage their own affairs. On the other, once they create a board, the stockholders are shackled. Id.
50. WYO. STAT. § 17-17-120 (b)(i) & (ii) (1989).
51. Id. § 17-17-121.
52. Id. An amendment to the corporation’s articles of incorporation eliminating the board must be approved by all of the shareholders. Id. at § 17-17-121(b). If after eliminating the board of directors the corporation decides to reinstate the board, it may do so by amending its articles of incorporation. Id. at § 17-17-121(d). The amendment must be approved by at least two-thirds (2/3) of the corporation’s shareholders. Id. The amendment must also specify the number, names and addresses of the corporate directors or describe who will perform the board’s duties. Id.
53. Id. § 17-17-121(c).
porate powers are to be exercised by and under the authority of the shareholders. The shareholders are authorized to manage the business and affairs of the corporation, and any actions which previously required director approval must now be authorized by shareholder approval.

The shareholders of a statutory close corporation may also enter an agreement to restrict the discretion or powers of the board of directors. Such an arrangement provides the shareholders with greater control, while still maintaining the corporate form and may be desirable in a corporation with too many shareholders to effectively allow the shareholders to run the corporation directly.

If the powers and discretion of the existing corporate board are restricted by agreement, then the directors are relieved of any liability imposed by law. To the extent that the agreement governs the powers or discretion of the board, liability is imposed on each person who assumes the board's power. A shareholder, however, is not liable for his act or omission, although a director would be, unless the he is entitled to vote on the action.

The Close Corporation Supplement allows shareholders to tailor management patterns to meet the specific needs of a family controlled business. The Wyoming Business Corporation Act also allows corporations with fifty (50) or fewer shareholders to eliminate the board of directors by amending its articles of incorporation. The articles of incorporation must describe who will perform some or all of the duties of the board. This requires the attorney to draft provisions providing that some person or group will perform the directors' duties, and to what extent that person or group while performing the directors' duties will be subject to liability.

Clearly, the Supplement provisions dealing with the elimination of the board of directors are more streamlined. The Supplement specifically addresses who takes over the boards responsibilities and liabilities. The Act, on the other hand, requires that these subjects be spelled out in the Articles of Incorporation, requiring additional drafting and increasing the possibility of error. If a corporation desires to operate without or to limit the authority of its board of directors election of statutory close corporation status is the better alternative.

54. *Id.* § 17-17-121(c)(i).
55. *Id.*
56. *Id.*
57. *Id.* § 17-17-120.
58. *Id.* § 17-17-120(c).
59. *Id.*
60. *Id.* § 17-17-121(c)(iii).
63. *Id.*
64. *Model Business Corp. Act* § 8.01 Official Comment.
C. Elimination of Corporate Bylaws

Another common requirement of corporate statutes which may be eliminated in close corporations is corporate bylaws.65 Corporate bylaws are a set of rules which govern the internal affairs of the corporation and regulate the management of the corporation. The bylaws may contain any provision for managing the business and regulating the affairs of the corporation, not inconsistent with the law or the articles of incorporation.66

In closely held corporations, where most or all of the investors are active in the business and the corporation operates on an informal basis, imposing the highly structured formalities contained in most bylaws would be cumbersome.67 Also, the provisions required in bylaws are often contained in the articles of incorporation or a shareholder agreement. Requiring the adoption of bylaws where the provisions are contained in other business agreements would require unnecessary duplication.68

While the Wyoming Business Corporation Act requires a corporation to adopt bylaws,69 the Supplement provides the means to eliminate this unnecessary duplication.70 A “statutory close corporation” may dispense with the bylaws if the provisions required by law are contained either in the articles of incorporation or a shareholder agreement.71 Once a “statutory close corporation” terminates such status,72 however, it is required to adopt bylaws immediately.73

D. Elimination of Corporate Annual Meeting

An annual shareholder meeting is another requirement of most corporate statutes which is not important in a closely held corporation. The principal purpose of an annual meeting is the annual election of directors and to vote on corporate business requiring shareholder approval. Where there are one or two shareholders who are active in the corporation’s day to day affairs, a formal annual meeting is unnecessary. Also where the board of directors has been eliminated there is no need for an annual election. Eliminating the annual meeting is beneficial under these circumstances.

Under the Wyoming Business Corporation Act a corporation is required to hold a meeting of the shareholders annually at a time stated

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65. Under the Wyoming Business Corporation Act the incorporators or the board of directors are required to adopt initial bylaws for the corporation. Wyo. Stat. § 17-16-206(a) (1989).
66. Id. § 17-16-206(b) (1989).
67. MODEL CLOSE CORP. SUPPLEMENT § 22 Official Comment.
68. Id.
70. Id. § 17-17-122.
71. Id.
72. Id. § 17-17-131.
73. Id. § 17-17-122(b). See, e.g., id. § 17-16-206.
or fixed in accordance with the bylaws.\textsuperscript{74} The Supplement, on the other hand, allows a "statutory close corporation" to dispense with holding an annual meeting, unless one (1) or more shareholders request a meeting.\textsuperscript{75} The Supplement only requires that the corporation set a date in case one of the shareholders demands an annual meeting.\textsuperscript{76}

For a corporation which desires to operate in an informal manner, the Supplement provision is attractive, as an annual meeting is a needless requirement. If the shareholders desire an annual meeting the Supplement provides for such flexibility. Elimination of the annual meeting is an attractive option provided by the Supplement.

\textbf{E. Protection Against Piercing the Corporate Veil}

As has been described, close corporations often operate in an informal manner. The corporation is run as a family-owned business with shareholders managing and operating the business. Often, these businesses are incorporated to provide the owners the protection of limited liability. Yet, in some cases, despite full compliance with state law governing the formation of the corporation, courts have imposed personal liability on the shareholders for failing to follow the requisite corporate formalities.\textsuperscript{77}

In many opinions, the courts focus on the failure of the corporation to follow normal corporate routine and then conclude that the corporation is the "alter ego" or an "instrumentality" of the shareholders and impose personal liability upon the shareholders.\textsuperscript{78} There appears to be a substantial risk of imposing personal liability on the shareholders when: shareholder meetings or directors' meetings are not held, decisions are made by shareholders as though they were partners, or complete corporate and financial records are not maintained.\textsuperscript{79}

The importance of corporate formalities tends to create a trap for unwary shareholders in close corporations. Shareholders in a small corporation often find managing the business a full time occupation and they often put off or ignore the corporate formalities. The play-acting aspects of corporate meetings, elections, and the like are often regarded by the businessmen as rather insignificant.

\textsuperscript{74} Id. \textsuperscript{22} 77-17-6-01(a). The failure to hold an annual meeting, however, does not affect the validity of any corporate action. Id. \textsuperscript{22} 77-17-6-01(c).
\textsuperscript{75} Id. \textsuperscript{22} 77-17-123(b). If a shareholder desires a meeting, he/she must deliver written notice to the corporation requesting a meeting at least thirty (30) days prior to the date set for the annual meeting. Id. \textsuperscript{22} 77-17-123(b).
\textsuperscript{76} Id. \textsuperscript{22} 77-17-123(a). Unless the corporation's articles of incorporation or bylaws, or a shareholder agreement provide otherwise, the annual meeting date is set by statute as the last day of the third month following the close of the business year. Id.
\textsuperscript{78} Bach, 222 Kan. 589, 567 P.2d 1337.
\textsuperscript{79} Miles v. CEC Homes, 753 P.2d 1021 (1988).
Electing close corporation status may protect shareholders from liability based on the corporations failure to observe usual corporate formalities. Generally close corporation statutes excuse corporations from observing corporate formalities. The Supplement provides that:

[T]he failure of a statutory close corporation to observe the usual corporate formalities or requirements relating to the exercise of its corporate powers or management of its business and affairs is not a ground for imposing personal liability on the shareholders for liabilities of the corporation. 80

The purpose of this section is to eliminate the possible argument that the shareholders in a statutory close corporation are individually liable for the debts and torts of the business because the corporation did not follow the classic model of a corporation. 81

This provision, however, does not prevent a court from imposing personal liability based on inadequate capitalization or commingling of assets. 82 A court may still “pierce the corporate veil” of a statutory close corporation “if the circumstances would justify imposing personal liability on the shareholders [if] the corporation [was] not a statutory close corporation.” 83

In a situation where it is foreseeable that the corporation will be operated on an informal basis, this protection is of the utmost importance. One of the main reasons for incorporating is the protection of limited liability. If after incorporation, a court imposes personal liability upon a shareholder for failing to observe corporate formalities, this purpose has been undermined. Therefore, in such a situation the corporation should choose statutory close corporation status and enjoy the protection from imposition of personal liability provided by the Supplement.

LIMITATIONS ON THE TRANSFER OF STOCK

A. Share Transfer Restrictions

Another advantage provided by the Close Corporation Supplement is the automatic restriction on the transfer of shares. 84 By their nature, closely held corporations are owned and operated by the same individuals. In order to maintain the ability to make business decisions with the least amount of formality, the owners of a close corporation need to be able to work together. Share transfer restrictions help insure that the owners of a close corporation can decide with whom they will work. 85

82. O'Neal, supra note 9, at § 1.17.
85. 2 O'Neal, supra note 9, § 7.02. O'Neal points out that, because of the close nexus between ownership and management, decisions in close corporations are made
Courts have recognized the desirability of share transfer restrictions in close corporations. In the past, however, courts have had to determine how broad transfer restrictions were intended to be. In so doing, courts often injected a requirement of "reasonableness" into valid share transfer restrictions. As a result, shareholders could not be sure if their share transfer restrictions would withstand a court challenge. The Supplement addresses this problem by prohibiting all transfers, whether voluntary or involuntary, of "shares of a statutory close corporation ... except to the extent permitted by the articles of incorporation . . . or a buy sell agreement . . . ." In addition, if an owner of shares subject to the transfer restriction desires to sell his shares, he first must offer the shares to the corporation. These provisions are designed to provide restrictions that fit the needs of the "typical" close corporation. They also facilitate alterations tailored to the special needs of shareholders in particular situations. The attorney is not faced with the job of drafting an absolute stock transfer prohibition, which most courts would probably hold invalid. Rather, his task under the Supplement is one of drafting the few, if any, narrow exceptions to the statutory stock transfer prohibition which the shareholders of the corporation may want.

It should be noted that certain transfers are explicitly exempt from the prohibition. It should also be noted, however, that these statutory exemptions can be abrogated by the articles of incorporation.

Often "with a minimum of formality" and without regard to the relative sizes of ownership interests of shareholders. "It is thus not surprising that shareholders in a closely held enterprise usually desire to retain the power to choose future associates." Id. (footnote omitted). O'Neil points to specific examples justifying the need for control over the transferability of ownership interests: where a shareholder is concerned about an outsider's integrity or business acumen; where shareholders are concerned about unfriendly competitors gaining access to records and voting rights through the unrestricted purchase of shares in the corporation; where shareholders want to guard against the concentration of control in any one shareholder; and where "the shareholders' active participation in the business is necessary to its success." Id.

86. See, e.g., Gray v. Harris Land and Cattle Co., 737 P.2d 475, 476 (Mont. 1987); see also 2 O'Neal, supra note 9, § 7.02.
87. See, e.g., Hill v. Warner, Bergman & Spitz, P.A., 197 N.J. Super. 152, 484 A.2d 344, 350-51 (1984) ("the unqualified restraint on the transfer of shares of stock is in contravention of public policy and void"); Renberg, 667 P.2d at 469 ("[n]Absolute restrictions forbidding the alienation of corporate stock are invalid, but reasonable restrictions are not.").
89. Id. § 17-17-112(a).
90. See 2 O'Neal, supra note 8, § 7.06 0.2 and accompanying text.
91. Wyo. Stat. § 17-17-111(b). The transfers not subject to the prohibition of § 17-17-111(a) include transfers: to the corporation or existing shareholders; to members of the shareholder's immediate family; to the shareholder's personal representative; or to "a trustee or receiver as the result of bankruptcy, insolvency, [or] dissolution . . . ." Id. Also, the restrictions do not apply: if the transaction was approved by all shareholders having general voting rights; if the transfer was made by merger, consolidation or share exchange (an exchange of existing shares for other corporate shares of a different class or series); if the transfer was made by pledge as collateral if the pledgee does not receive any voting rights; or if the transfer was made after the corporation terminated its "statutory close corporation" statutes. Id.
92. Id.
Thus, eliminating these exemptions will expand further the scope of the statutory prohibition against the transfer of shares of a close corporation. \(^93\)

Although the shares in a statutory close corporation are subject to an automatic share transfer restriction, the shareholders do have the ability to transfer their shares. A shareholder wishing to sell shares which are subject to the share transfer restriction contained in the Supplement must first offer his or her shares to the corporation.\(^94\) To meet this requirement, the shareholders must offer the shares to the corporation first by obtaining an offer to purchase from an "eligible" third person.\(^95\) After receipt of the offer from the eligible third person, the shareholder must deliver the offer to the corporation.\(^96\) This delivery constitutes the requisite offer by the shareholder to sell all of his or her shares to the corporation under the terms of the offer from the eligible third person.\(^97\) Following the offer of shares to the corporation, a special shareholders' meeting must be held to decide whether the corporation should purchase the offered shares.\(^98\)

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\(^{93}\) Presumably, this would be a fairly easy task. While \(§ 17-17-111(a)\) does not automatically prohibit transfers to a shareholder's immediate family because of the exception of \(§ 17-17-111(b)(i)\), the articles of incorporation could specifically override this exception and prohibit such a transfer merely by stating that the prohibition of \(§ 17-17-111(a)\) will apply to transfers to a shareholder's immediate family, notwithstanding the exception of \(§ 17-17-111(b)(i)\).

\(^{94}\) Id. \(§ 17-17-112\).

\(^{95}\) Id. \(§ 17-17-112(a)\). An eligible person is defined as one who:

[i] . . . is eligible to become a qualified shareholder under any federal or state tax statute the corporation has adopted and . . . agrees in writing not to terminate his qualification without the approval of the remaining shareholders; . . . and

[ii] . . . [whose] purchase of the shares will not impose a personal holding company tax or similar federal or state penalty tax on the corporation.

\(^{96}\) Id. \(§ 17-17-112(b)\). The third person's offer must be in writing and state the offeror's name and address, the number and class or series of the shares offered to be purchased, the offering price per share, and other terms of the offer. Id. \(§ 17-17-112(a)\).

\(^{97}\) Id. \(§ 17-17-112(c)\).

\(^{98}\) Id. The offer constitutes an offer to sell all of the offering shareholder's stock in the corporation, and therefore, the corporation must decide whether to purchase all or none of the offered shares. Id. If the corporation decides to accept the offer, it must deliver written notice of acceptance to the offering shareholder within seventy-five days of the corporation's receipt of the offer. Id. \(§ 17-17-112(d)\). The offer is deemed rejected if this written notice is not given. Id. \(§ 17-17-112(d)\). An affirmative vote of a majority of the votes entitled to be cast at the meeting (excluding any votes associated with the offered shares) is required for acceptance of the offer. Id. \(§ 17-17-112(c)\). If the corporation accepts the offer, the offering shareholder must deliver the duly endorsed certificates to the corporation within twenty days of the date of acceptance. Id. If the shares are not represented by certificates, the shareholder must instruct the corporation to transfer the shares on the books of the corporations. Id. If the shareholder fails to deliver the certificates, "[t]he corporation may specifically enforce the shareholder's . . . obligation . . . ." Id. If, on the other hand, the corporation rejects the offer, the offering shareholder, for a period of 120 days after the corporation receives the offer, has the opportunity to transfer all of the offered shares to the eligible third person. Id. \(§ 17-17-112(f)\). Again, the shareholder can only transfer all or none of the shares. Id.

In addition, the corporation may make a counteroffer. Id. \(§ 17-17-112(d)\). If the shareholder wishes to accept the counteroffer, he or she must give written notice of acceptance within fifteen days of the receipt of the counteroffer. Id.
Any attempted transfer which is binding on the third party transferee, and which is in violation of the statutory transfer provisions, is ineffective. An attempted transfer which is not binding on the transferee, either because of lack of notice or because a court refuses to enforce the prohibition, gives the corporation an option to purchase the shares from the transferee under the same terms as he acquired the shares.

In contrast to the automatic share transfer restrictions contained in the Supplement, Wyoming’s general corporation statute allows a corporation to put restrictions on the transfer of shares, but does not provide for the restriction automatically. Instead, share transfer restrictions of a corporation organized under the general corporate statute must be drafted into “[t]he articles of incorporation, bylaws, an agreement among shareholders, or an agreement between shareholders and the corporation . . . .”

While the Supplement’s share transfer restrictions may not appear to be significantly different from what is available under the general corporate statutes, the lawyer must approach the problem of share transfer restrictions from different directions under the different statutes. As stated earlier, under the Close Corporation Supplement, the lawyer’s job involves the drafting of the desired exceptions to the statutory share transfer restriction and its exemptions. His job under the general corporate statute involves drafting share transfer restrictions from scratch.

The significance of this difference is apparent considering how courts have treated share transfer restrictions. Generally, courts will invalidate absolute transfer restrictions, accepting as legitimate only those restrictions which are reasonable. This places upon the corporate attorney the unpleasant duty of attempting to draft a share transfer...
restriction which clearly and unambiguously covers every conceivable transfer intended to be restricted. The attorney should remember that courts generally will resolve an ambiguity in a share transfer restriction against the restriction and in favor of the free alienability of property. Thus, the attorney for the corporation organized under the general corporate statute needs to avoid drafting a restriction which could be viewed as an absolute restraint on the alienability of property.

However, the general aversion to restrictions on the free alienability of property has less significance in the context of a close corporation's share transfer restrictions. This is reflected in the legislative decision to enact a close corporation statute which contains automatic restrictions on the transfer of shares. This interpretation of the close corporation supplement's share transfer restrictions is consistent with the general purpose of close corporation statutes—to provide freedom and flexibility to small, closely held corporations which previously were governed by general corporate statutes designed to meet the needs of the publicly held corporation. The decision to include automatic share transfer restrictions in the close corporation supplement should be viewed as a legislative determination that transfer restrictions are inherently reasonable in the context of a close corporation.

Although transfer restrictions are automatic under the Close Corporation Supplement, the restrictions are not absolute. There exist in the Supplement exceptions to the automatic restrictions on share transfers. However, the corporation is given the option of abrogating these exceptions in the articles of incorporation. Therefore, shareholders could face a share transfer restriction which is even broader than the automatic transfer restriction contained in the Supplement.

Given the purpose behind the enactment of close corporation statutes, any attempt to impose restrictions beyond those provided in the statute arguably should not face intense judicial scrutiny. The same


107. The courts' general approach of viewing share transfer restrictions with suspicion could reflect a more basic concern with allowing too much flexibility to those doing business in the corporate form. With no restrictions on shareholders' ability to control the corporation and its ownership, the corporation begins to look more like a partnership. While the Close Corporation Supplement has as one of its goals increased flexibility, see supra notes 6-7 and accompanying text, absolute flexibility would blur the distinction between partnerships and corporation to a point where the only identifiable difference, outside of the tax field, would be the existence or nonexistence of limited liability. Thus, even under the Supplement, shareholders may be faced with unfavorable responses from the courts to shareholders' attempts to maintain absolute control over the ownership and operation of the corporation.


110. Id.
concerns of reasonableness of restrictions which have occupied courts in the past should not threaten the validity of transfer restrictions in the context of a statutory close corporation. The legislature has determined that broad share transfer restrictions are inherently reasonable in close corporations, and has given express authority to the corporation to make the statutory restrictions even broader.

B. Buy-Out Agreements

In addition to general share transfer restrictions, shareholders of close corporations often make use of buy-out agreements to provide for the compulsory purchase by the corporation of the shares of deceased shareholders. The close corporation supplement has special provisions relating to buy-out agreements. If the articles of incorporation so provide:

[T]he personal representative of the estate or the surviving joint tenant of the deceased shareholder may require the corporation to purchase or cause to be purchased all . . . of the decedent’s shares or jointly owned shares or to be dissolved.

If a close corporation elects to include this statutory buy-out provision, it can be modified only if the modification is set forth or referred to in the articles of incorporation.

Buy-out agreements are especially attractive to close corporations for one very important reason. Normally, there is no established market for the shares of a close corporation; therefore, the corporation or other shareholders are the only prospective purchasers of the shares of a deceased shareholder. This is particularly important when the deceased was a minority shareholder. Like other limitations on the transfer of stock, however, the drafting of a buy-out agreement (or clause in the articles of incorporation) can be a complicated task absent the statutory provisions contained in the Close Corporation Supplement.

By electing the stock buy-out provision of the Supplement, the shareholders can avoid the troubles of entering into a private agreement. Election also eliminates the problems raised when the shareholders

111. See, e.g., Hill, 484 A.2d at 350-51; Renberg, 667 P.2d at 469.
113. Id. § 17-17-114.
114. Id. §§ 17-17-114(a) & (b). At least two-thirds (2/3) of the shareholders must approve the inclusion, modification or deletion of the provision in the articles of incorporation. Id. § 114(c). For purposes of this provision, the term "shareholders" refers to the holders of the votes of each class or series of shares of the statutory close corporation, voting as separate voting groups, whether or not otherwise entitled to vote on amendments. If the corporation has no shareholders when the amendment is proposed, it must be approved by at least two-thirds (2/3) of the subscribers for shares, if any, or, if there are no subscribers, by all the incorporators. Id.
115. See 2 O’Neal, supra note 9, § 7.26.
116. Id.
117. Id. § 1.17.
118. Model Close Corporation Supplement § 14 Official Comment.
have entered into a buy-out agreement, but have failed to agree on a price formula, or have agreed on a formula but have left out other necessary terms.\textsuperscript{119} These problems are avoided through the election of the statutory buy-out provisions. The compulsory purchase right can be enforced even if the shareholders have failed to agree on a formula for determining the purchase price or have failed to provide other necessary information.\textsuperscript{120} Even if the corporation has elected to be governed by the statutory buy-out provisions, a shareholder may waive his (and his estate's) rights under the provisions.\textsuperscript{121}

If the compulsory purchase right is provided for in the articles of incorporation, a person wishing to exercise that right\textsuperscript{122} must first deliver written notice of the intent to exercise the right to the corporation within 120 days after the shareholder's death.\textsuperscript{123} Within sixty (60) days after the effective date of the notice, a special shareholders meeting must be held to determine whether the corporation should offer to purchase the shares.\textsuperscript{124} If it is decided that the corporation should offer to purchase the shares, the offer must be delivered in writing to the person requesting the purchase within seventy-five (75) days after the effective date of the notice.\textsuperscript{125} This offer must be accepted within fifteen days after receipt, or it will be considered rejected.\textsuperscript{126}

The price and terms which are fixed or to be determined by the articles of incorporation, bylaws, or written agreement will govern the compulsory purchase.\textsuperscript{127} In the event that the corporation defaults on its obligation to purchase the shares, the person exercising the compulsory purchase right may force a dissolution of the corporation through state district court.\textsuperscript{128} If the corporation rejects the purchase offer or makes no offer, the person exercising the compulsory purchase right may compel purchase through the courts.\textsuperscript{129}

\textsuperscript{119} Id.
\textsuperscript{120} Wyo. Stat. § 17-17-116. In a proceeding to enforce a compulsory purchase right, the court is directed to determine the fair market value of the shares in accordance with id. § 17-17-142. For further discussion of share purchase rights, see infra notes 144-52 and accompanying text.
\textsuperscript{121} Wyo. Stat. § 17-17-114(e). This waiver must be in writing signed by the shareholder. Id. A shareholder may also enter into a separate agreement providing for the purchase of his shares at the time of his death. Id. § 17-17-114(f).
\textsuperscript{122} The persons who may exercise the right are limited to the personal representative of the deceased shareholder and the surviving joint tenant. Id. § 17-17-114(a).
\textsuperscript{123} Id. § 17-17-115(a). The requisite notice must describe the number and class or series of shares, and must request that the corporation offer to purchase the shares. Id.
\textsuperscript{124} Id. § 17-17-115(b).
\textsuperscript{125} Id. § 17-17-115(c). Any offer made by the corporation must be accompanied by corporate financial information. Id. This information must include a "balance sheet as of the end of a fiscal year ending not more than sixteen (16) months before the effective date of the request notice, an income statement for that year, a statement of changes in shareholders equity for that year, and the latest available interim financial statements, if any." Id.
\textsuperscript{126} Id.
\textsuperscript{127} Id. § 17-17-115(e).
\textsuperscript{128} Id.; see also id. § 17-17-116(a).
\textsuperscript{129} Id. § 17-17-116.
In a proceeding seeking to compel purchase the court is required to determine the fair market value of the shares by considering relevant evidence as to:

[T]he going concern value of the corporation, any agreement among some or all of the shareholders fixing the price or specifying a formula for determining share value for any purpose, the recommendations of appraisers, if any, appointed by the court, and any legal constraints on the corporation's ability to purchase the shares. 130

After determining the fair market value of the shares, the court will order the corporation to purchase the shares or cause the purchase of the shares. 131 The court may also empower the person exercising the compulsory purchase right to have the corporation dissolved. 132

While the Close Corporation Supplement, as discussed above, provides specific guidelines governing buy-out agreements, the general corporate statute has no such provision. For a corporation organized under the general corporate statute, buy-out provisions must be drafted into the articles of incorporation, bylaws or separate agreements among shareholders, or between shareholders and the corporation. These types of clauses or agreements will be governed by the same provision of the general corporate statute as are other limitations on the transfer of shares. 133

This then raises the same problem discussed in the previous section—lawyers are forced to draft buy-out provisions not knowing how a court will interpret them. If the shareholders of a corporation organized under the general corporate statute want to have a buy-out agreement, that agreement likely will be drafted by the corporation's attorney. Like share transfer restrictions, buy-out agreements are essentially restraints upon the alienability of property. As such, the corporation's attorney must draft them carefully so as to avoid a court determination that the buy-out provision is unreasonable. 134

It appears that these provisions only make life easier for the attorney. However, these flexible provisions really inure to the benefit of the corporation and the corporation's shareholders. In the case of corporations which "are not particularly complicated, election of close corporation status may avoid costs that would otherwise be incurred in drafting a more complicated shareholders buy-out agreement." 135 Significant savings can be realized by avoiding the need to draft complicated limitations on the transfer of stock by taking advantage of the

130. See id. § 17-17-142(b)(i).
131. Id. § 17-17-116(b). The corporation may petition the court to modify the terms of the purchase order based on a change in financial or legal ability of the corporation or other purchaser to complete the purchase. Id. § 17-17-116(c).
132. Id. § 17-17-116(b).
133. See id. § 17-16-627.
134. See supra notes 105-09 and accompanying text.
135. 2 O'NEAL, supra note 9, § 1.17 (footnote omitted).
provisions included in the Close Corporation Supplement. In addition, with legislatively developed standards, courts are not forced to determine the reasonableness of potentially endless variations of attempted limitations on the transfer of stock of closely held corporations.

**Remedies**

In addition to the provisions previously discussed, the Supplement also contains significant remedial provisions. These provisions provide remedies beyond those provided in general corporate statutes to close corporations and minority shareholders faced with board deadlocks or “squeeze-outs” and other oppressive conduct of controlling shareholders. They also will serve as detailed guides to courts faced with disputes between a close corporation and its shareholders.

A shareholder of a statutory close corporation may petition the court for ordinary relief, forced share purchase, or dissolution if:

(i) those in control of the corporation are acting in a manner that is illegal, oppressive, fraudulent or unfairly prejudicial;
(ii) those in control of the corporation are deadlocked in the management of the corporation's affairs; or
(iii) grounds exist for judicial dissolution under W.S. § 17-16-143.

The relief applied is based on a progressive analysis. The court first looks to ordinary relief and evaluates its adequacy. If ordinary relief is inadequate, then the court may order share purchase or dissolution. It should be noted that, in contrast to the Model Close Corporation Supplement position, these remedial provisions were not intended to be exclusive.

**A. Ordinary Relief**

If the court finds that one or more of the grounds listed above exist, it may order such relief as it deems appropriate including, but not limited to, those listed in section 17-17-141(a). The specific types of relief:

(i) the performance, prohibition, alteration or setting aside of any action of the corporation or of its shareholders, directors, or officers or any other party to the proceedings;
(ii) The cancellation or alteration of any provision in the corporation's articles of incorporation or bylaws;
relief are listed in an effort to overcome the reluctance some courts have shown in the past in ordering anything other than dissolutions and buy-outs.  

B. Extraordinary Relief—Share Purchase

If the court finds that the ordinary relief is or would be inadequate or inappropriate, it may order that the corporation be dissolved. In the alternative, the corporation or one or more of the shareholders may purchase all of the aggrieved shareholder’s shares at their fair market value. If the court orders a share purchase, it shall: 1) determine the fair market value of the shares; 2) specify the terms of the purchase; 3) require the seller to deliver the shares to the purchaser upon receipt of the purchase price; 4) provide that the seller has no further claim against the corporation; and 5) provide that if the purchase is not completed as to the terms, the corporation will be dissolved.

C. Extraordinary Relief—Dissolution

The court may dissolve the corporation if judicial grounds exist under the general corporate statute, or if all other relief ordered by the court has failed to resolve the dispute. The court may consider the financial condition of the corporation in determining whether to

(iii) The removal from office of any director or officer;
(iv) The appointment of any individual as a director or officer;
(v) An accounting with respect to any matter in dispute;
(vi) The appointment of a custodian to manage the business and affairs of the corporation;
(vii) The appointment of a provisional director who has all the rights, powers and duties of a duly elected director to serve for the term and under the conditions prescribed by the court;
(viii) The payment of dividends; or
(ix) The award of damages to any aggrieved party.

Id.

147. Id.
148. Id. § 17-17-142(b)(i). The court is required to consider the going concern value of the corporation, any agreement fixing a price or specifying a formula to determine the value, appraiser’s recommendations, and any legal constraints on the corporation’s ability to purchase the shares. Id.
149. Id. § 17-17-142(b)(ii).
150. Id. § 17-17-142(b)(iii).
151. Id. § 17-17-142(b)(iv).
152. Id. § 17-17-142(b)(v). If the corporation is dissolved, the selling shareholder has the same rights and priorities in the corporation’s assets as if the sale had not been ordered. Id. § 17-17-142(d).
153. Id. § 17-17-143(a)(i). The grounds for dissolution under the general corporate statute are found at id. § 17-16-1430.
dissolve the corporation, but may not refuse to dissolve solely because the corporation has accumulated earnings or current operating profits.155

CONCLUSION

The new Wyoming Close Corporation Supplement provides numerous advantages over the general corporate statutes for small business enterprises which desire to incorporate. The special provisions contained in the Supplement are not designed to be the answer to all business organization questions, but may fit the needs of many closely held enterprises in Wyoming. The flexibility provided by the statute will allow the unsophisticated business to conduct its operation without risking loss of the limited liability which corporate status affords the owners of a business.

Part of this flexibility is evidenced by the Supplement's explicit acceptance of shareholder agreements. This provision recognizes the reality that the small businesses do not and cannot operate in the same manner as large publicly owned corporations. It also recognizes the precarious position in which a minority shareholder may find himself or herself. With explicit recognition of the validity of shareholder agreements, the Supplement provides the minority shareholder with what may be the only possible avenue for protecting that which in many instances is the shareholder's major personal asset. The Supplement also allows for the elimination of the board of directors, corporate bylaws and annual meetings. As the owners of a small business also generally perform the management functions, making decisions on a daily basis, these formal requirements, if required, are of little substance. In the past, by ignoring corporate formalities, owners of close corporations have set themselves up for personal liability. For corporations choosing to elect close corporation status, the failure to follow traditional corporate formalities no longer threatens the limited liability enjoyed by shareholders.

Much of the flexibility provided by the Supplement can also be attained by a corporation organized under the general corporate statutes. However, the Wyoming Close Corporation Supplement provides this flexibility at a lower cost. The Supplement accomplishes this cost savings by eliminating the need for drafting certain complex provisions for inclusion in the articles of incorporation, bylaws and agreements among the parties. The Supplement's share transfer restrictions provide uniform protection to close, family-run businesses which want to control ownership of the corporation. The buy-out provisions, likewise, provide guidance in planning the disposition of otherwise unmarketable shares upon a shareholder's death. Finally, the Supplement provides expanded, detailed remedies, which give shareholders added security, and provide courts with statutory authority to order remedies which they previously have proved reluctant to use.

155. Id. § 17-17-143(b).
By recognizing the special needs of small business enterprises, the Wyoming Close Corporation Supplement provides a viable alternative to incorporation under the general corporate statutes. Incorporation under the Wyoming Business Corporations Act will continue to be the best choice for many Wyoming businesses. However, the Supplement offers a special kind of flexibility of which a number of small enterprises can take advantage at considerably less cost and risk.

JAMES BELL GILPIN
WILLIAM K. ROUNSBORG